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C O N F I D E N T I A L SECTION 01 OF 02 TOKYO 004556

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SUBJECT: JAPAN ECONOMIC AGENDA: FUKUDA STARTS WITH DOMESTIC  
POLICIES

Classified By: Ambassador J. Thomas Schieffer for reasons 1.4 b/d

#### Summary

11. (C) Japan's new Prime Minister Yasuo Fukuda has kept the Abe administration's economic team largely intact, but there are indications that policy focus has shifted toward domestic pocketbook issues. Former finance minister Sadakazu Tanigaki's appointment suggests a commitment to fiscal restraint. The prospects for reform are unclear, although we may get a better sense from Fukuda's policy speech to the Diet October 1. End Summary.

#### Same Team, Shifted Priorities

12. (SBU) Having run within the Liberal Democratic Party (LDP) on a platform stressing "stability," newly elected Prime Minister Yasuo Fukuda made almost no changes to former PM Abe's economic team. The key exception was the appointment of former Finance Minister Sadakazu Tanigaki as LDP Policy Research Council Chairman.

13. (C) Despite the familiar faces, Fukuda's press remarks and initial instructions to cabinet ministers suggest greater attention on domestic economic issues. While efforts to extend Japan's support of refueling operations in the Indian Ocean will be Fukuda's first and most pressing task, Fukuda has made clear his intent to tackle the pocketbook issues Japanese voters have ranked among their top concerns, including addressing regional economic disparities.

14. (C) Fukuda is well-known for playing his cards close to the vest, and his economic agenda remains vague. His initial statements as prime minister, however, have centered on a number of fixes to current systems, including freezing already slated increases in medical premiums for older patients, repairing the much-criticized pension records system, revitalizing regional economies, studying tax rate

changes, and tightening political fundraising regulations. Notably absent from his initial remarks has been discussion of Japan's economic partnership agreements (their version of free trade agreements), regional economic architecture, the Doha Development Round, and encouraging foreign direct investment into Japan.

#### Refilling the Trough?

15. (C) Fukuda's repeated mention of regional disparities, along with the LDP's loss of rural voters in July's Upper House elections, has led some to speculate the LDP will return to pork barrel spending. But Fukuda's appointment of Tanigaki, a known budget hawk, suggests the contrary -- a commitment to fiscal conservatism and the goal of reaching primary budget balance by 2011. Tanigaki was also a strong advocate of a consumption tax increase during the 2006 LDP presidential campaign.

16. (C) What about reform? Given the continuing popularity of former PM Koizumi's "reform agenda" in polls (at least as a slogan), Fukuda will continue to express his support. Moreover, many on the team -- including Fukuda -- have reform credentials. But there has been no indication so far of a "big idea" animating the reform agenda, and Council on Economic and Fiscal Policy (CEFP) Minister Ota told the press her first discussion with PM Fukuda included notice that reforms proposed in the CEFP's most recent policy blueprint -- which many found relatively tepid -- would be subject to revision.

#### Comment

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17. (C) PM Fukuda has described his cabinet as having its "back to the wall," with no margin for error. While there may be support for reform among cabinet members as individuals, Fukuda's focus on fixing domestic programs -- an agenda thrust on the LDP by the opposition -- suggests a defensive emphasis on competence rather than a desire to pursue bold new initiatives.  
Schieffer